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APR 22 1991

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

Federal Communications Commission
Office of the Secretary

In the Matter of)
)
Petitions for Declaratory) MMB File No. 910221A
Ruling Regarding Reversionary) MMB File No. 870921A
and Security Interests)

To: The Commission

COMMENTS OF SANTARELLI, SMITH & CARROCCIO

A. Thomas Carroccio
Nathaniel Rayle
SANTARELLI, SMITH & CARROCCIO
1155 Connecticut Avenue, N.W.
Suite 900
Washington, D.C. 20036
202/466-6800

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SUMMARY

The law firm of Santarelli, Smith & Carroccio supports the petition for declaratory ruling which seeks the rescission of the Commission's prohibition on security interest in broadcast licenses.

The legislative history of the Communications Act clearly supports the contention that a broadcast licensee has a vested property interest in its license. Therefore, the Commission is free to rescind the prohibition previously promulgated by it.

The current state of the broadcast financial marketplace compels the rescission of the prohibition on security interests. Such rescission has the potential to reinvigorate broadcast lending and, therefore, would be in the public interest.

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The law firm of Santarelli, Smith & Carroccio ("SS&C" or "Firm") hereby submits its comments in the captioned declaratory ruling proceeding.^{1/} For its comments, SS&C states as follows:

I. SECURITY INTERESTS

A. Industry Conditions Compel The Rescission Of
The Commission's General Prohibition On Security
Interests In Broadcast Authorizations

1. Over the past several years, the Firm has served as counsel to a number of commercial banks and finance companies lending, or considering lending, to the broadcast industry. Such representation has provided the Firm with insight as to the impact the Commission's policy against the collateralization of broadcast authorizations has had upon both the individual loan decisions of established broadcast lenders, and the decisions of certain other financial institutions to refrain from extending loans to broadcasters. On the basis of its experience, the Firm believes

^{1/} Petition for Declaratory Ruling filed by the law firm of Hogan & Hartson, MMB File No. 910221A ("Petition"), and Motion for Declaratory Ruling filed by the law firm of Crowell & Moring, MMB File No. 870921A ("Motion").

the relief sought by the Petition would serve both to encourage further extensions of credit by current broadcast lenders, and to provide an incentive for other financial institutions to begin or resume making loans to the broadcast industry.^{2/}

2. The inability to obtain a direct security interest in what is, in effect, a broadcaster's single most valuable asset, has long been a significant negative factor in every lender's credit analysis of a proposed broadcast loan. Although a lender may obtain an indirect lien on a broadcast license through the pledge of either stock or partnership interests in a licensee entity, such a pledge mechanism cannot provide the lender any priority over the licensee's other creditors with regard to the value which could be derived from the authorization. A lender also must recognize that those broadcast assets in which it may obtain a security interest (e.g., equipment) are subject to radical devaluation in the event they are separated from the license authorizing their use. Recent

^{2/} Although this issue is being considered in a Mass Media proceeding and is framed in the context of broadcast licenses, the underlying principles are equally applicable to all communications services regulated by the Commission. Broadcast licensees are not the only ones adversely affected by the current credit shortage. The holders of authorizations for other services, and prospective purchasers of such authorizations, also are severely hampered by the unavailability of credit to support their business plans. For example, equipment manufacturers are now the main source of credit for the cellular industry, and their credit requirements are becoming increasingly selective. In addition, they have almost totally ceased providing credit for cellular acquisitions. The Commission should give serious consideration to promulgating its declaratory ruling on the Petition so that its effect clearly extends to all authorizations issued by the Commission, without regard to the service for which they are issued.

bankruptcy court decisions^{3/} have only served to heighten lenders' concerns regarding the implications of their inability to obtain interrelated security interests in all of a broadcast licensee's assets.

3. The unique risk factors associated with broadcast lending have long limited the number of lenders willing to extend credit to the broadcast industry. Now, when coupled with the general economic downturn and universal credit shortage, these factors are causing the virtual disappearance of credit from the broadcast marketplace. Today, only a few finance companies remain willing and able to consistently provide financing to broadcasters.

4. It is imperative that the Commission re-examine its current prohibition on security interests in its authorizations with an eye towards the removal of that ban. Although such action, by itself, may not restore the broadcast capital markets to full health, it will provide a significant incentive to both present and potential sources of broadcast loans.

B. The Present Prohibition On Security Interests
In Broadcast Authorizations Is Not Mandated By
The Communications Act And May Be Rescinded By
The Commission

5. SS&C agrees with the Petition's contention that the Communications Act of 1934, as amended ("Act"), contains no provision which would act as a bar to a lender obtaining a security interest in a broadcast license. The prohibition on security

^{3/} E.g., In re Oklahoma City Broadcasting Co., d/b/a KGMC-TV, Debtor, 112 Bankr. 425 (Bankr. W.D. Okla. 1990).

interests was created solely by the Commission and, therefore, may be rescinded by the Commission without any prior action by Congress.

6. In the first specific articulation of its policy prohibiting security interests in broadcast licenses, the Commission simply stated that "[t]he extraordinary notion that a station license issued by this Commission is a mortgageable chattel in the ordinary commercial sense is untenable." Radio KDAN, Inc., 11 F.C.C.2d 934, 12 R.R.2d 584, 585 n.1 (1968). Upon reconsideration of that decision, the Commission reaffirmed its position and further opined as follows:

The Commission has consistently held that a broadcast license (as distinguished from a station's plant or physical assets) may not be hypothecated by way of mortgage, lien, pledge, lease, etc. This principle, deriving ultimately from Section 301 of the Communications Act, is firmly rooted in Commission practice, its rationale being that such a hypothecation endangers the independence of the licensee who is and who should be at all times responsible for and accountable to the Commission in the exercise of the broadcasting trust.^{4/}

This language makes clear that the present policy barring security interests in broadcast licenses had its genesis in the Radio KDAN case, and was premised upon the Commission's interpretation of the Act.

7. An examination of the then extant Commission precedent, however, reveals that such a "principle" was neither "deeply

^{4/} Radio KDAN, Inc., 13 R.R.2d 100, 102 (1968).

rooted" nor "consistently held" prior to Radio KDAN.^{5/} As pointed out in the Petition, the Commission had previously stated that a creditor could not rely upon a Commission-issued license as an asset from which to satisfy a licensee-debtor's obligations, but such statements had been premised on the fact that such licenses are at risk of being revoked or denied renewal. See Twelve Seventy, Inc., 6 R.R.2d 301, 304 (1965). Prior to Radio KDAN, the Commission had never stated what is now the basis for its policy against security interests in broadcast licenses, i.e., that a license "is not an owned asset or vested property interest so as to be subject to a mortgage, lien, pledge, attachment, seizure, or similar property right." Kirk Merkley, Receiver, 94 F.C.C.2d 829, 54 R.R.2d 68, 70 (1983), recon. denied, 56 R.R.2d 413 (1984).

8. In 1968, the Commission cited Section 301 of the Act as compelling the policy against security interests. Radio KDAN, 13 R.R.2d at 102. By 1983, the Commission was citing Sections 301, 304, 309(h) and 310(d) in support of the policy. Kirk Merkley, 54 R.R.2d at 70. Sections 301, 304 and 309(h) each act to bar the vesting in a licensee of any right to the use of a specific frequency or channel.^{6/} Section 310(d) requires prior Commission

^{5/} It would appear the inaccurate citation to extensive precedent may have arisen out of the fact that the security interest at issue in the Radio KDAN cases was, in effect, a reversionary interest against which the Commission then had, and continues to have, a long-standing and well-articulated prohibition.

^{6/} Section 301 provides for "the use of such channels, but not the ownership thereof...." Section 304 requires a licensee to sign

consent to any assignment of a license, or to the transfer of control of a licensee. None of these statutory provisions, or any other provision of the Act, in any way prohibits considering a license or other authorization, as opposed to a channel or frequency, as a property interest. In fact, SS&C believes the legislative history of the Act provides clear evidence that a license or other authorization should be considered a property interest of its holder.

9. As part of its 1952 amendment of the Act, Congress modified what is now Section 310(d) so as to prohibit comparative challenges to assignment or transfer applications.^{2/} When setting forth the purposes of the amendment to Section 310(d), the Senate

^{6/} (...continued)
of the electromagnetic spectrum...." Section 309(h) provides that a license shall not vest in the licensee "any right in the use of the frequencies designated in the license...."

^{2/} The text of 47 U.S.C. § 310(d), with the pertinent 1952 amendment language underlined, is as follows:

Section 310(d). No construction permit or station license, or any rights thereunder, shall be transferred, assigned, or disposed of in any manner, voluntarily or involuntarily, directly or indirectly, or by transfer of control of any corporation holding such permit or license, to any person except upon application to the Commission and upon finding by the Commission that the public interest, convenience and necessity will be served thereby. Any such application shall be disposed of as if the proposed transferee or assignee were making application under Section 308 for the permit or license in question; but in acting thereon the Commission may not consider whether the public interest, convenience and necessity might be served by the transfer, assignment, or disposal of the permit or license to a person other than the proposed transferee or assignee.

specifically acknowledged a licensee's property interest in its license. The Senate report on the 1952 amendments states, in part, as follows:

One of the purposes of the proposed new language in this subsection is to annul the so-called Avco procedure adopted several years ago by the Commission to prevent a licensee from selling his property to a proper person of his choice by requiring an opportunity for others to make bids for any radio station proposed to be sold. The Committee believes that there is no provision of present law which authorizes the Commission to employ such a procedure and it deems such procedure an unwise invasion by a government agency into private business practice.^{8/}

10. That Congress wanted to remove an unwarranted impediment to a licensee's transfer of its "property" (i.e., its license or permit) is clearly and unequivocally stated. Because Section 310(d) applies to the transfer or assignment of a "construction permit", as well as a "station license", the language of the Senate report cannot be construed as referring to "property" other than a Commission authorization.^{2/} By clarifying a licensee's right to sell "his property to a proper person of his choice," Congress, a fortiori, was affirming the existence of the licensee's property right in the license. This clear congressional recognition of a licensee's or permittee's property right in its broadcast

^{8/} S. Rep. No. 44, 82d Cong., 1st Sess. (1951) (emphasis added).

^{2/} It should be noted that the 1952 amendments to the Act also added construction permits to the purview of Section 310(d)'s predecessor. Accordingly, the Congress must be viewed as knowing it was referring only to authorizations when it used the term "property." See, S. Rep. No. 44, supra note 7.

authorization must take precedence over the Commission's subsequent determination that such an authorization "is not an owned asset or vested property interest."^{10/}

11. Since its initial promulgation in Radio KDAN, the Commission's prohibition on security interests in broadcast authorizations has been premised on the mistaken belief that the Act prohibits the vesting in an authorization holder of any property interest in its broadcast authorization. As demonstrated above, however, the Act does not bar such vesting of property interests, but instead, actually recognizes a licensee's property interest in its license. The Commission, therefore, has full discretion, unfettered by any provision of the Act, to now reexamine and rescind the policy it created regarding security interests in broadcast licenses. The Firm urges the Commission to use the opportunity of this proceeding to remove the blanket prohibition on security interests in broadcast authorizations and, thereby, to help alleviate the severe credit shortage currently afflicting the broadcast industry.^{11/}

^{10/} Kirk Merkley, 54 R.R.2d at 70.

^{11/} To the extent the Commission deems it necessary to either guard against specific perceived abuses associated with security interests, or otherwise protect certain vital public interests, it can adopt specific rules or policies tailored to meet such issues. For example, the Commission adopted Section 22.917(e) of the Rules to prevent a lender from repossessing cellular equipment in which it has a security interest without first providing both the Commission and the affected cellular licensee at least ten days advance written notice of any seizure of the equipment.

C. The Commission Should Specify Mechanisms And
Procedures Upon Which Licensees And Creditors
May Rely With Regard To Security Interests

12. In order for any rescission of its prohibition on security interests in broadcast licenses to be meaningful, the Commission also must provide broadcast licensees and lenders with guidance as to appropriate mechanisms and procedures to be utilized in the perfection of, and execution upon, such security interests. As indicated in the Petition, the Uniform Commercial Code ("UCC") provides a basic framework upon which the Commission, licensees and lenders may rely. Appropriate judicial proceedings also provide support for the management of security interests in broadcast licenses. However, the Commission must consider how those existing procedures interact with its own regulatory mandate.

13. Perfection of Security Interests. SS&C cautions the Commission against setting itself up as a national "recorder of deeds" with regard to security interests in broadcast licenses. The Commission is not presently equipped to establish priorities of creditors' claims, and should not expend its limited resources to do so. Instead, the Commission should allow its licensees and their creditors to rely upon the established and proven mechanisms

provided by each state's commercial code.^{12/} In addition, the Commission should continue to rely upon the courts for the resolution of contractual disputes involving broadcast licenses, including any disputes as to the priorities of conflicting creditors' claims. Of course, the Commission may wish to require licensees to also file copies of such UCC filings with the Commission pursuant to Section 73.3613(b) of the Rules.

14. Assignment or Transfer of Broadcast Licenses Upon Execution on Security Interests. In most instances, a licensee, upon defaulting on a loan agreement, can be expected to cooperate with its secured lender in the execution on the associated security interest. In such a situation, the parties may utilize standard Commission procedures to obtain consent to any assignment or transfer of license necessitated by the default. In some cases, however, a licensee-debtor may attempt to utilize the formalities and delays inherent in the regulatory process as tactical weapons in the economic battle with its creditors. The Commission should provide secured lenders with appropriate relief from this type of situation.

^{12/} The Commission should allow a UCC filing regarding a security interest in a broadcast license to include any future "modification, extension or renewal" of that license. Although such language could appear to extend the secured party's interest in the license beyond the remaining license term, the secured party's interest would be subordinate to the requirements of the Act and the Commission's Rules, and would be effective only if the continuation of the license was found by the Commission to be in the public interest.

15. One form of relief the Commission should consider is allowing a licensee and its lender to appoint an independent trustee as part of the establishment of a security interest in a license. Upon default by the licensee-debtor, the independent trustee would be able to file an application seeking Commission consent to the involuntary assignment of the license to the trustee for the purpose of maintaining the collateral, including the license, and arranging for its sale, upon obtaining Commission consent, to a qualified purchaser. The Commission has condoned the use of a privately appointed trustee to effectuate a two-step, involuntary then voluntary, acquisition by a qualified purchaser.^{13/} Such a procedure also would be appropriate for facilitating an involuntary execution upon a security interest in a broadcast license.

16. As an additional or alternative procedure, the Commission should consider allowing a licensee-debtor to specifically provide a secured lender the remedy of seeking court appointment of an independent receiver, who could then follow the two-step procedure specified above for maintaining the collateral, including the license, and arranging for its sale.

17. The ability to perfect, and efficiently execute upon, a security interest in a broadcast license will provide a substantial degree of comfort to otherwise chary lenders. Such comfort, in

^{13/} Tender Offers and Proxy Contests, 51 Fed. Reg. 9794, 59 R.R.2d 1536 (1986), appeal dismissed for want of ripeness sub nom. Office of Communication of the United Church of Christ v. Federal Communications Commission, 826 F.2d 101 (D.C. Cir. 1987).

turn, cannot help but to increase the availability of loans to the broadcast industry.

II. REVERSIONARY INTERESTS

18. The Firm does not take any position as to whether the Commission should remove its present absolute prohibition on a broadcast station seller regaining control of the station in the event of the purchaser's default under a financing agreement with the seller, provided the seller first obtains Commission consent for the reacquisition of control. However, if the Commission creates an exception to its rule against reversionary interests, it should be careful that it does not imbue seller financing with any aura of priority. The priority of creditors should be left to negotiations among the affected private parties, and to the operation of state and federal laws regarding the rights of creditors. To do otherwise may upset the already tenuous balance among broadcast creditors and, thereby, having a chilling effect on the willingness of third party lenders to extend credit in such situations.

III. CONCLUSION

The Commission has an opportunity to bring a new level of stability to the financing of broadcast stations at a time when such stability is sorely needed as a catalyst to the recovery of the broadcast credit marketplace. In light of the clearly expressed intent of Congress on the matter of property interests in broadcast authorizations, the Commission should not feel

constrained by any restrictive interpretation of the Act previously promulgated by its predecessors. Accordingly, the Commission should move expeditiously to rescind its present blanket prohibition on security interests in broadcast licenses. At the same time, the Commission may want to grant some limited relief to sellers who finance the sale of their stations, but should avoid any pronouncement which may have the effect of upsetting the present schedule of priorities among broadcast creditors.

Respectfully submitted,

SANTARELLI, SMITH & CARROCCIO

By: 

A. Thomas Carroccio
Nathaniel Rayle
SANTARELLI, SMITH & CARROCCIO
1155 Connecticut Avenue, N.W.
Suite 900
Washington, D.C. 20036
202/466-6800

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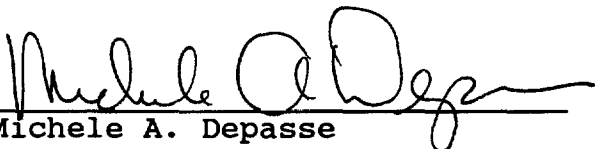
CERTIFICATE OF SERVICE

I, Michele A. Depasse, a secretary with the law firm of Santarelli, Smith & Carroccio, do hereby certify that on this 22nd day of April, 1991, a true and correct copy of the foregoing "Comments of Santarelli, Smith & Carroccio" was delivered by U.S. mail, first-class, postage-prepaid to the following individuals:

Roy J. Stewart, Esquire
Chief, Mass Media Bureau
Federal Communications Commission
1919 M Street, N.W.
Room 314
Washington, D.C. 20554

Marvin J. Diamond, Esquire
Gardner F. Gillespie, Esquire
Susan Wing, Esquire
Hogan & Harton
555 - 13th Street, N.W.
Washington, D.C. 20004

Victor E. Ferrall, Jr., Esquire
John T. Scott, III, Esquire
Crowell & Moring
1001 Pennsylvania Avenue, N.W.
Washington, D.C. 20004-2505


Michele A. Depasse